IN THE HIGH COURT OF JUDICATURE AT BOMBAY

ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX REFERENCE NO. 37 OF 1990

The Commissioner of Income-tax,
Bombay City-VI, Bombay. ... Applicant.

V/s.

M/s.Maganlal Chaganlal P.Ltd.
C/o. Standard Drum & Barrel Mfg.Co.
Govan Pada Village,
Chembur, Bombay - 400 074. ... Respondent.

Mr.Ashok Kotangale for the applicant.

Ms.Asifa Khan for the respondent.

CORAM : V.C.DAGA AND A.S.AGUIAR, JJ.

DATED : 30th September 2005.

ORAL JUDGMENT : (Per V.C. Daga, J.)

. This reference under Section 256(1) of the Income-Tax Act, 1961 ("Act" for short) is at the instance of the Revenue, arising out of the order in I.T.A.No.2848/Bom/1984 dated 16th November, 1987 passed by the Income-Tax Appellate Tribunal, Mumbai ("the Tribunal" for short) for the Assessment Year 1975-76 whereby the following substantial questions of law has been referred for the opinion of this Court :-

(1) Whether on the facts and in the circumstances of the case, the Tribunal was right in law in holding that where the

assessee is a dealer in shares and holds certain shares as stock-in-trade, the interest paid by the assessee on the funds borrowed for the purpose of investment in such shares is to be allowed as admissible deduction u/s. 36(1)(iii) and not under section 57(1)(iii) ?

(2) Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that where the assessee is a dealer in shares and holds certain shares as stock-in-trade, the interest paid by the assessee on the funds borrowed for the purpose of investment in such shares is not to be reduced from the gross dividend while granting relief u/s 80 M?

The Facts :
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2. The assessee-company derives income from business of manufacturing drums and barrels and dealing and speculation in shares. During the year under consideration, the assessee received, by way of dividend, an income of a sum of Rs.13,35,454/- and claimed deduction under section 80M of the Act on the entire amount. The Income Tax Officer ("I.T.O." for short) worked out the interest attributable to the borrowed funds for acquisition of shares at Rs.25,80,801/- and adjusted the same against the dividend income. He further allocated a sum of Rs.29,246/-, which according to him, represented expenses incurred for the purpose of earning dividend income. The result was that there was no positive income under the head "dividend income" and consequently, he denied the assessee's claim under section 80M.

3. The Commissioner of Income Tax (Appeals) ("C.I.T.(A)" for short), in the appeal filed at the instance of the assessee, granted partial relief. The C.I.T.(A) worked out the interest attributable to the investment in shares at Rs.3,22,528/- payable on a sum of Rs.25,59,020/-, being the borrowed funds utilised for acquisition of shares in M/s.Killick Nixan Ltd. and M/s.British Burma Petroleum Ltd. The balance interest was allowed by the C.I.T.(A) under section 36(1)(iii) on the ground that the interest was admissible as a deduction under section 36(1)(iii) of the Act being payment in respect of sums borrowed for the purpose of business in share dealings. In doing so, C.I.T.(A) relied on the decision of the Gujarat High Court in the case of **C.I.T. v. Cotton Fabrics Ltd.**, (1981) 131 ITR 99 (Guj).

4. In the appeal preferred by the Revenue before the Tribunal, the order passed by C.I.T.(A) came to be confirmed. The Tribunal held that the Supreme Court decision in the case of **Distributors (Baroda) Pvt.Ltd. v. Union of India**, (1985) 155 ITR 120 (SC), relied upon by the Revenue, did not apply to the facts of the case.

Rival Submissions :
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5. Learned Counsel appearing for the Revenue reiterated the submissions made before the Tribunal and placed reliance on the judgment of the Apex Court in the case of **Distributors (Baroda) Pvt.Ltd.** (supra). He further submits that in the case of assessee itself, for the assessment year 1968-69, the very same question, may be in a little different form, was considered by this Court in its judgment reported in (1999) 236 ITR 456 (**C.I.T. v. Maganlal Chhaganlal (P.) Ltd.**). He submits that in that case, while dealing with more or less similar question, the Division Bench of this Court held that the deduction under Section 80M of the Act has to be calculated with reference to the amount of dividend computed in accordance with the provisions of the Act forming part of the gross total income, i.e., after deducting interest paid on monies borrowed for earning such income, and not with reference to the full amount of dividend received by the assessee. He, thus, submits that the question raised in the case of assessee, once again, is no more open for debate. He further submits that the aforesaid judgment of this Court in the case of assessee, for the assessment year 1968-69, has become final and conclusive and, therefore, it would not be reasonable or proper for this Court to take contrary view in the case arising

out of the order meant for the subsequent assessment year 1975-76.

6. Per contra, learned counsel appearing for the respondent-assessee urged that the amount of interest paid on the overdraft and the expenses incurred to earn the income, related to the business of trading in shares, have to be allowed as deduction in computing income under the head "business" and the expenses should be deducted from the dividend income granting deduction under section 80M of the Act.

The Issue :
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7. The issue for consideration is:-

> "Whether or not the interest paid on borrowings used for the purchase of shares held by the respondent-assessee should not be reduced from the dividend income granting deduction under section 80M or it should be treated as business expenditure incurred for trading in shares?"

Consideration :
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8. Having heard rival parties, before dealing with rival submissions, we must point out that the assessee is a private limited company carrying on

business of manufacturing of drums and barrels and also dealing in shares and making investments in shares.

9. In the case of assessee itself for the assessment year 1968-69, deduction under section 80M of the Act had been calculated with reference to the amount of dividend computed in accordance with the provisions of the said section forming part; of the gross total income, i.e. after deducting interest on monies borrowed for earning such income, and not with reference to the full amount of dividend received by the assessee [see C.I.T. v. Maganlal Chhaganlal (P.) Ltd., (1999) 236 ITR 456].

10. The aforesaid judgment of the Division Bench of this Court presided over by Justice B.P.Saraf (as he then was) in the case of respondent-assessee itself had been delivered following the judgment of the Apex Court in the case of **Distributors (Baroda) P.Ltd.** (supra). The said judgment has been accepted by the respondent-assessee.

11. Apart from the above, the main business of the respondent-assessee herein is not to deal in shares and stocks but to manufacture drums and barrels. Thus, the case of the assessee is fully

covered by the ratio of the decision of the Supreme Court in the case of **Distributors (Baroda) P.Ltd.** (supra); wherein it has been held that deduction under section 80M(1) of the Act has to be calculated with reference to the amount of dividend computed in accordance with the provisions of the Act forming part of the gross total income, i.e., after deducting interest paid on monies borrowed for earning such income, and not with reference to the full amount of dividend received by the assessee.

12. At this juncture, it will not be out of place to mention that in Income Tax Reference No.117 of 1989 (*C.I.T. v. M/s.Emrald Co.Ltd.*), which has been decided by us along with the reference at hand, we did permit the respondent-assessee therein to claim deduction of interest paid on overdraft and the expenditure incurred relating to the business of trading in shares treating it as allowable expenditure under the head "business" since the sole business of the assessee therein M/s.Emrald Co.Ltd. (supra) was to deal in shares and stocks only. The income from dividend was an incidental income. In that view of the matter, it is not possible for us to follow the judgment delivered by us in the case of M/s.Emrald Co.Ltd. (supra). The said judgment can be distinguished on fact. The view taken in the case at hand is based on the fact that the

respondent-assessee's main business is not of dealing in shares and stocks but they are basically engaged in the business of manufacture of drum and barrels. According to us, this is a crucial distinguishing feature between the case of the present respondent-assessee (M/s.Maganlal Chhaganlal P.Ltd.) and that of M/s.Emrald Co.Ltd. (supra).

13. Thus, in the facts and circumstances of this case, we answer both questions referred to us in the negative, i.e., in favour of Revenue and against the assessee.

. Reference stands disposed of with no order as to costs.

(A.S.AGUIAR, J.) **(V.C.DAGA, J.)**